# Report on the Evaluation of Bonding in the Non-Energy Solid Minerals Program

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|---|---|
| Program: | Non-Energy Solid Mineral Leasing regulated by 43 CFR 3500 |
| Work Process Evaluated: | Administration of Performance Bonds |
| Responsible Assistant Director: | Minerals, Realty and Resource Protection |
| Dates Conducted: | June 18, 2001 through August 30, 2001 |

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## Executive Summary

The Washington Office (WO) of the Bureau of Land Management (BLM) is responsible for ensuring that BLM programs operate in compliance with law, regulations and policy. The WO uses periodic evaluations as a means of program quality control. The WO has received anecdotal evidence that the bonds on file for the non-energy leasable minerals program do not meet current policy and, in some cases, bond amounts are substantially less than what would be needed to cover reclamation costs should permitees or lessees default on their obligations. As a result, the WO selected the bonding aspect of non-energy mineral leasing program for an evaluation. This evaluation is intended to document the extent of any problems with bonding and develop recommendations for correcting any problems that may be identified. This document reports the results of the bonding evaluation.

On June 18, 2001 WO issued Instruction Memo (IM) 2001-168 to the State Directors of Arizona (AZ), California (CA), Colorado (CO), Eastern States (ES), Idaho (ID), Montana (MT), New Mexico (NM), Nevada (NV), Utah (UT), and Wyoming (WY), requesting information concerning bonds on file for the non-energy leasable minerals program. These States were selected because they have leases issued for non-energy leasable minerals. The WO evaluated the information submitted by each State Office to determine if their respective bonding practices and bond amounts conformed to the 43 CFR 3500 regulations published on October 1, 1999. The BLM considers the cost of complying with all the terms of the permit or lease, including rental, royalty and reclamation provisions when setting the bond amount required by 43 CFR 3504.50.

All permittees and lessees of non-energy mineral resources are required to post bonds to ensure compliance with permit and lease terms and conditions. Bonds are required by 43 CFR 3504.50 and administered under the standards given in 43 CFR 3504.51 through 43 CFR 3504.71 (64 FR 53546, 10/1/1999). Specific program policies are established in BLM Manual Section 3504 released 2/18/1988. Data standards for the program are described Washington Office Instruction Memorandum 95-129, 5/22/1995. It is also BLM policy that all bonds must be reviewed annually to ensure adequacy and adjusted where necessary.

The evaluation was coordinated by Philip Allard of the Solid Minerals Group assisted by Scott Murrellwright of the Phoenix Field Office. Each State Office was responsible for collecting and reviewing the data they submitted for this evaluation. The evaluation was conducted by individuals in each affected office who were most familiar with the program. No field visits were made. This required the evaluation to be conducted from the review of the information in our existing systems.

The evaluation determined that there are few problems in this program. The problems that were identified are limited in scope but will require attention. Most of the problems that were identified in the draft report have already been corrected so references to these have been dropped from the final report on the evaluation. Revisions to the BLM Manual and the program data standards are recommended. The following items remain to be resolved:

- The WO should update BLM Manual 3504 released on 2/18/1988. The revision needs to incorporate the current 43 CFR 3504 regulations that became effective on October 1, 1999. Six States have provided comments about their bond review process and suggestions for changes to the manual. These comments and suggestions are shown in Appendix 1 and should be taken into account during the manual revision process. The revised manual should resolve the policy issue raised by Idaho about using a per acre reclamation schedule endorsed by State government instead of an estimate of the cost of reclamation based on the assumption that BLM has to complete reclamation through contracts.

- The WO should revise the LR2000 data standards to ensure that appropriate data is entered in the system. The evaluation identified that all States were following the data standards, but the standards were found to be ambiguous in certain areas. These ambiguities need to be resolved. Also, the Automated Bond and Surety System has recently been integrated into LR2000. The current data standards do not reflect this, so the standards need revision.

- WO should meet with the New Mexico State Office to continue the discussion of New Mexico's concerns about the bonding policy. New Mexico should consider preparing decisions addressed to the potash mine operators designed to bring the bonds for these operations into compliance with BLM Manual Section 3504. The draft decisions could consider phased implementation or other methods to reduce financial shocks to the industry. BLM management could then review these draft decisions and determine if it is feasible to issue them.

- WO should monitor the emerging crisis in the surety bond market. News reports indicate that bonding companies and reinsurers have received significant financial shocks from the 9/11 attacks and the Enron and Kmart bankruptcies. Industry has reported to BLM that surety premiums are escalating rapidly and some companies have been unable to obtain bond coverage. Some surety companies are withdrawing from the market. This could make it difficult for New Mexico to resolve the bonding problems in their program through the use of traditional surety methods or the other bond instruments listed in the regulations at 43 CFR 3504.55.

**Program Information**

Program being evaluated: Non-Energy Leasable Minerals

Offices being evaluated: Arizona, California, Colorado, Eastern States, Idaho, Montana, New Mexico, Nevada, Utah, Wyoming State Offices and Field Offices with bonding responsibilities as determined by the State Offices

| Budget program names: | Subactivities: |
|---|---|
| Other Mineral Resources | 1330 |

Strategic Goals:

01.02 Provide Opportunities for Environmentally Responsible Commercial Activities

01.02.01 By FY 2005, complete 80% of actions on existing energy and mineral leases, permits, and claims on the Federal lands while meeting established land health standards and minimizing future liabilities.

Annual performance goals:

01.02.03.02 Number of Federal non-energy and other mineral post -authorization actions

Work processes:

Use Authorization
Implementation

Program elements:

EO

Last evaluation date:

There have been no previous evaluations of this aspect of the non-energy leasable mineral program

This program evaluation is needed to assure BLM management that commercial development of the public land is environmentally responsible.

**Evaluation Objectives and Scope**

This evaluation is intended to document the extent of any problems with bonding and develop recommendations for correcting any problems that may be identified. In addition to evaluating the bonding program, this evaluation will review BLM's ability to produce necessary management information about bonding from our existing systems.

This evaluation was limited to the management of performance bonds in the non-energy leasable mineral program. The Arizona, California, Colorado, Eastern States, Idaho, Montana, New Mexico, Nevada, Utah, Wyoming State Offices participated in the evaluation conducted from June 18 through August 30, 2001. These State Offices were involved in the evaluation because they have activity in this program area. Some of the State Offices involved Field Offices they selected. The involvement of Field Offices was at the discretion of the State Offices because not all State Organizations manage their bonding programs in the same way. Also, not all Field Offices have activity in this program.

**Methodology**

Ten states were asked to provide the information on bonding in the non-energy mineral leasable program in tabular form and describe the adequacy of the bonds in four categories:

- Number of bonds that are 25% or less of the recommended amount,
- Number of bonds between 25% and 50% of the recommended amount,
- Number of bonds between 50% and 75% of the recommended amount, and
- Number of bonds 75% or more of the recommended amount.

In this evaluation bonds falling below 75% of the recommended amount are considered to be deficient and in need of adjustment.

A draft report on the bonding evaluation was prepared and it found that of the 103 bonds reported by the State Offices, 89 or 86% of the bonds are 75% or more of the recommended amount. The remaining 14 bonds (14%) needed to be adjusted. The data submitted by the State Offices is presented in Appendix 1 and summarized in a table in Appendix 2.

The WO sent the draft report to the State Offices for review as an attachment to Instruction Memorandum 2002-90 (IM) on February 7, 2002. This IM provided the State Offices an opportunity to review the draft findings of the Washington Office and, if necessary, suggest changes so that the final report more accurately describes the status of their programs.

For this evaluation only authorized Federal leases were considered. Prospecting permits, and terminated leases reported by the states were not included in this analysis. The WO checked a random sample of the data in the LR2000 system and found no significant inconsistencies between the data reported and the data in LR2000. Bureau of Indian Affairs (BIA) Indian mineral lease and reclamation bonds were not included in this evaluation because BLM does not hold or administer these bonds.

**Areas of Positive Performance**

Seven of the ten states reviewed stated that they refer to BLM Manual 3504 for guidance when establishing bond amounts. The 3504 Manual requires that bonds be based on three months royalty on production, annual rental, and estimated reclamation cost. Since annual rental payments can be recouped from royalty payments it is not required to add three months of royalty payments and the annual rental together if the amount of three months of royalty exceeds the annual royalty.

In this evaluation WO considered bonds within 75% of the estimated bond amount to be satisfactory. It is possible to estimate three months of rental and royalty payments with a fair amount of precision by considering the receipts from previous years. However, it is difficult to estimate future reclamation costs. An engineering estimate for a project will often have about a 10% error. Reclamation estimates have additional error because one also needs to anticipate the future conditions of the mine site when the reclamation takes place. These conditions cannot be known with precision and add to the error of the engineering estimate. In this evaluation WO considered the States to be in substantial compliance with BLM policy, and within the error of the estimate of reclamation costs, if the bonds on file are 75% or more of the amount required by the policy. This allows BLM to focus its limited resources on addressing those situations that are out of substantial compliance with BLM policy.

Chart 1

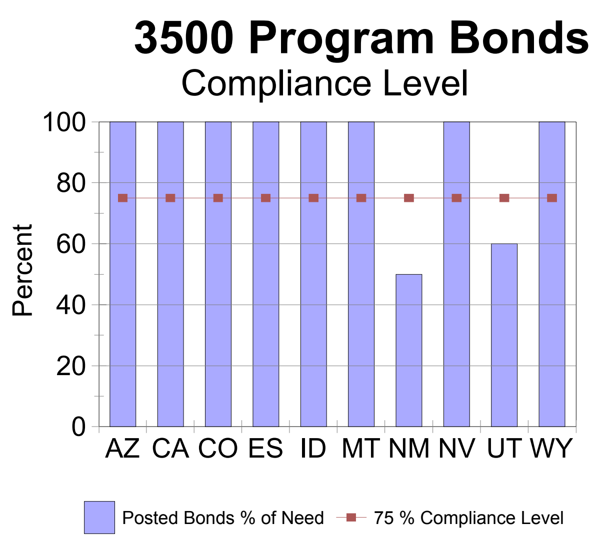


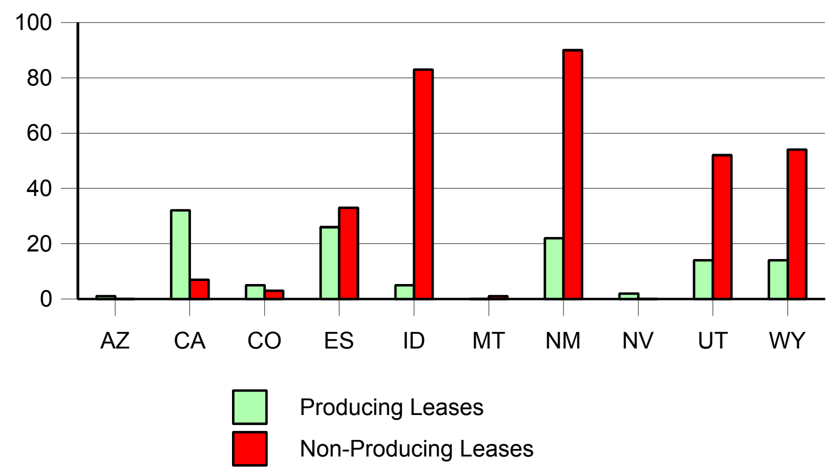

Chart 1 shows the percentage of bonds in a given State that meet or exceed 75% of the required bond amount. Eight States exceeded the bond amount of 75% used in this analysis. In fact, these eight States met 100% of their estimated bond requirements.

All of the States reported that they review and adjust the bond amounts if needed.

Chart 2 shows the number of producing and nonproducing leases in each of the States. The States that lack adequate bond coverage do not have significantly more producing or nonproducing leases than some other States that report adequate coverage. This indicates that work load is not the principal cause for these two states failing to meet the bonding policy set out in the Manual. Instead, it may be a result of placing priority on other aspects of this program or on other programs.

Producing and Non-Producing Leases

Chart 2.




According to one State the current BLM bonding procedures have worked well. In contrast, another State has indicated that the entire bonding system needs to be revised to include a broad array of new bond instruments and other forms of financial guarantees. This evaluation indicates that eight out of the ten states meet or exceed the recommended bonding level. This suggests that even though the manual needs to be revised to reflect the current 43 CFR 3500 regulations, the procedures outlined in the 3504 BLM Manual (2/18/88) are still effective.

This evaluation indicates that the BLM as a whole is in compliance with the 43 CFR 3504 bonding regulations. The regulations and manual work when they are put to use. Of the 103 bonds on file 90 or 88% are 75% or more of the total amount needed to cover estimated reclamation costs and 1/4 of estimated royalty and rent.

**Opportunities for Improvement**

The evaluation indicated that four bonds held by BLM are not adequate to cover 1/4 of the estimated annual production royalty. The draft evaluation report noted that in some cases there was adequate reclamation bonding but still insufficient bonding to cover 1/4 of the estimated annual production royalty . This was because the reclamation liability was bonded through the State government for an amount higher than the BLM estimated cost and BLM only held a minimum lease bond. This is inconsistent with the 3504 manual. Appendix 1, Page 1, I., Procedures for Other Solid Mineral Leases which states in part:

> "it is incumbent on the Authorized Officer to carefully monitor development on solid mineral leases and ensure that the amount of the lease bond is sufficient for reclamation or that any cooperative agreement clearly states that the reclamation bonds held by a State for Federal leases are only to be used for reclamation costs associated with those Federal leases".

This also means that BLM must maintain, at a minimum, a bond for all leases to sufficiently cover 1/4 of the estimated annual production and royalty since bonds held by State government are only held for reclamation purposes.

Since the draft report was released, Idaho has corrected two situations where insufficient bonding was held to cover 1/4 of the estimate of annual royalties and rental by requiring the lessees involved to submit increased bonds. Utah also has issued three decisions increasing bond amounts. One of these decisions has been appealed and bonds were submitted in response to the other two decisions.

California reported that one lease is in default. California is using the bond associated with this lease to meet minimum royalties and rental requirements. There is no significant surface disturbance on this lease requiring reclamation.

Two States, New Mexico and Utah, are working to correct their bond deficiencies. Utah estimated that it would require 20 work hours and $500 of the budget to bring 10 of their deficient bonds into compliance provided the necessary bond decisions are not appealed. The State Office does not anticipate that further extensive negotiations over the bond amounts will be needed to resolve the bonding issues in these cases.

New Mexico is concerned that significantly increasing the bonds for two potash companies under their jurisdiction could have dramatic impacts on the financial viability of the companies' operations. The possibility exists that the financial strain of increasing the bonds could result in reduced ore recovery which is not in the interest of the conservation of the mineral resource.

A lack of support by management or a shortage of properly trained personnel could contribute to problems with bonds. It is also possible that bonding problems have developed over a long period of time and that the size of a bond based on three months royalty on production, annual rental, and estimated reclamation cost has dramatically escalated since the last time the bonds were adjusted.

**Appendices**

Appendix 1
State Evaluation Data and Comments
State Responses to the Draft Evaluation Report are Shown in Bold Text

<u>Arizona</u>

Leases & Bonds

| Number of Leases | Producing Leases | Non-Producing Leases | Statewide Bonds | Individual Bonds | Leases In Default |
|---|---|---|---|---|---|
| 1 | 1 | 0 | 0 | 1 | 0 |

Arizona has one sodium lease (fringe) consisting of 3.91 acres. The well producing the sodium is located on the adjacent private land so reclamation costs for this lease are minimal.

Bond Percent of Need

| Number of Bonds | Bond ≤24% of Need | Bond 25-49% of Need | Bonds 50-74 % of Need | Bonds 75-99 % of Need | Bonds ≥100 % of Need | Bonds/BLM < 100 % of Need for (Production/Royalty) |
|---|---|---|---|---|---|---|
| 1 | 0 | 0 | 0 | 0 | 1 | 0 |

<u>Arizona Comments:</u> None

LR2000: Serial Register page did not indicate bond amount, which does conform to current data standards.

<u>California</u>

Leases & Bonds

| Number of Leases | Producing Leases | Non-Producing Leases | Statewide Bonds | Individual Bonds | Leases In Default |
|---|---|---|---|---|---|
| 39 | 32 | 7 | 2 | 4 | 1* |

* CALA 0137519 is in default. The bond is being used for minimum royalties and rentals because there is no significant surface disturbance requiring reclamation.

Bond Percent of Need

| Number of Bonds | Bond ≤24% of Need | Bond 25-49% of Need | Bonds 50-74 % of Need | Bonds 75-99 % of Need | Bonds ≥100 % of Need | Bonds/BLM < 100 % of Need for (Production/Royalty) |
|---|---|---|---|---|---|---|
| 6 | 0 | 0 | 0 | 0 | 6 | 0 |

Note: A statewide bond covers IMC Chemicals for a total of $3,694,000 (43 CFR 3504.56). The reclamation bond is calculated for the mine as a whole rather than on a lease by lease basis. It is sufficient for royalties, rentals and reclamation and is recalculated annually. IMC Chemicals has a separate state reclamation (SMARA) bond due to the mixed land ownership consisting of private lands and federal mineral leases.

<u>California's Comments:</u>

- State bonding: When a solid leasable mineral operation is entirely on federal land, we share a joint reclamation bond with the state agency. This will avoid double bonding for reclamation provided the state bond is sufficient. However, we still need a BLM only bond for the royalties and rents. State agencies manage the surface only and do not bond royalties and rentals.

- State bonding and mixed ownership. When a solid leasable mineral operation is on mixed ownership including private lands and federal mineral leases, we may wish to have a BLM only reclamation bond if significant reclamation liability exists on the federal lands. However, if the state reclamation bond is sufficient for both federal and private lands in the mine, we can be a co-signatory for the reclamation bond but still need a BLM bond for the royalties and rentals.

- Royalty bond: I suggest an initial six month (rather than three month) royalty bond due to the time frame involved in issuing a noncompliance for back royalties, appeal rights, and the time required to coordinate between the MMS and BLM. For operators in good standing with producing leases this could be kept at three months.

- Rental bonds: I suggest a six month (rather than three month) royalty bond due to the time frames described above. Again for operators in good standing with producing leases this could be kept at three months.

- Statewide bonds: Some operators have statewide bonds that cover multiple leases rather than on a lease by leases basis. This is preferable provided that the bond includes sufficient coverage for all leases. The bonding policy should be revised to reflect that many companies have a statewide bond in conformance with current regulations (43 CFR 3504.56). However, the bond instrument should clearly state whether the BLM statewide bond is for royalties and rentals only, as in the case where a joint BLM-SMARA bond exists for reclamation; or whether the statewide bond is a BLM only bond for royalties, rental and reclamation.

<u>WO Comments:</u> BLM Manual 3504 (2/18/88) is still in effect. Appendix 1, Page 1, I. states in part

that "it is incumbent on the Authorized Officer to carefully monitor development on solid mineral leases and ensure that the amount of the lease bond is sufficient for reclamation or that any cooperative agreement clearly states that reclamation bonds held by a State for Federal leases are only to be used for reclamation costs associated with those Federal leases". Therefore, it is incumbent on BLM to maintain, as a minimum, a sufficient bond to cover royalties and rental. California's program is in compliance with the manual.

LR2000: Random check of serial register pages. Current data standards are being used in the cases checked.

Colorado

Leases & Bonds

| Number of Leases | Producing Leases | Non-Producing Leases | Statewide Bonds | Individual Bonds | Leases In Default |
|---|---|---|---|---|---|
| 8 | 5 | 3 | 1* | 4 | 0 |

* Bond amount includes bonds held by BLM, EPA, and Colorado Division of Minerals and Geology.

Bond Percent of Need

| Number of Bonds | Bond ≤24% of Need | Bond 25-49% of Need | Bonds 50-74 % of Need | Bonds 75-99 % of Need | Bonds ≥100 % of Need | Bonds/BLM < 100 % of Need for (Production/Royalty) |
|---|---|---|---|---|---|---|
| 5 | 0 | 0 | 0 | 0 | 5 | 0 |

Colorado's Comments:

Bonds are based on three months royalty production, annual rental, and estimated reclamation cost. Bonds are reviewed whenever there are major changes in production, new surface disturbance, change in ownership or lease renewal.

LR2000: Random check of serial register pages. Current data standards are being used in the cases checked.

Eastern States

Leases & Bonds

| Number of Leases | Producing Leases | Non-Producing Leases | Statewide Bonds | Individual Bonds | Leases In Default |
|---|---|---|---|---|---|
| 59* | 26 | 33 | 3 | 19 | 0 |

* 70 leases reported. 11 were prospecting permits and were not included in evaluation.

Bond Percent of Need

| Number of Bonds | Bond ≤24% of Need | Bond 25-49% of Need | Bonds 50-74 % of Need | Bonds 75-99 % of Need | Bonds ≥100 % of Need | Bonds/BLM < 100 % of Need Production/Royalty |
|---|---|---|---|---|---|---|
| 22 | 0 | 0 | 0 | 0 | 22 | 0 |

Eastern States Comments: The required bond amount is reviewed annually and set according to the Bureau Manual 3504.

WO Comments: It appears that the bond on file with BLM for case file VAES 003031 is in need of adjustment to cover at least 1/4 of the annual production/royalty. **Eastern States replied in their review of the draft report that the WO was in error. This lease has a $44,000 bond on file and, because reclamation is proceeding well, has a bonding need of less than this amount. They anticipate that some portion of this bond may be released in the near future.** In the draft report WO had indicated that there were 4 leases in Arkansas with bonds that were less than 100% of need. **Eastern States Office showed that WO misunderstood the way Eastern States Office calculated bond requirements. This lead WO to believe certain operations did not meet the bonding requirements. Eastern States rounds the amount of bond needed to cover reclamation up to the nearest whole thousand. There are small, intermittent operations on these leases to recover quartz crystals. These operations need little additional bonding to cover royalty. Adequate bonding for these operations is provided when the reclamation bond is increased to the nearest whole thousand and no adjustment to these bonds is needed**. WO has changed the table and the charts in the final report from the draft report to show that Eastern States is in full compliance with the bonding requirements in this program area.

LR 2000: Random check of serial register pages. Current data standards are being used in the cases checked.

Idaho

Leases & Bonds

| Number of Leases | Producing Leases | Non-Producing Leases | Statewide Bonds | Individual Bonds | Leases In Default |
|---|---|---|---|---|---|
| 88 | 5 | 83 | 10 | 12 | 0 |

Bond Percent of Need

| Number of Bonds | Bond ≤24% of Need | Bond 25-49% of Need | Bonds 50-74 % of Need | Bonds 75-99 % of Need | Bonds ≥100 % of Need | Bonds/BLM < 100 % of Need Production/Royalty |
|---|---|---|---|---|---|---|
| 22 | 0 | 0 | 0 | 0 | 12 | 0 |

Idaho's Bond Review Process/Comments:

BLM holds annual operations meetings with each of the lessees. Each company presents their current mine operation, areas mined and reclaimed, and discusses mining plans for the coming year including surface disturbance and reclamation.

Based on these meetings and the monthly inspections of the mines, the Pocatello Field Office staff makes needed adjustments to the bond levels for the various companies. Information on bond adjustments is relayed to the Idaho State Office Branch of Land and Minerals. The adjudicative staff coordinates with the State of Idaho under terms of the existing MOU to determine the amount of the bond the State holds for reclamation on Federal phosphate leases and requests bond increases from individual lessees based on the data received from the Pocatello Field Office and the State of Idaho. Up-dates are made to LR2000 and the Automated Bond and Surety System to reflect bond increases and bond reviews.

Bond adjustments are usually not required during the rest of the year because the companies have outlined all their plans for expansion and reclamation at the annual operations meetings.

Bonding is figured using the following criteria:

- Bonding required for inactive/non-producing leases (to cover rental and minimum royalty).

- Bond required for production is calculated on the anticipated production for the coming year as reported by the companies at the annual meeting. The production bond is computed using the guidelines in BLM Manuel 3504 - one fourth(1/4) of the yearly production times the current royalty per ton.

- Current bond required for reclamation is calculated on a formula of $300.00 per acre for the lands reclaimed but not released and $1800.00 per acre for un-reclaimed acreage. **Idaho reports that they are reconsidering this policy. These per-acre bond amounts are consistent with the MOU that Idaho BLM has with the State of Idaho, but Idaho BLM is concerned that these amounts may be inadequate. In one recent review of a mine extension Idaho required the company to have a third party prepare an estimate of the cost of reclamation as if BLM were to complete reclamation by contract. This estimate will provide the basis for revising current bond amounts.** There are very few individual phosphate lease bonds. Most of the phosphate leases bonds are statewide bonds which cover all of the lessee's Federal phosphate operations in the state. In accordance with 43 CFR 3504.5 Idaho BLM has a MOU with the Forest Service (FS) and the State of Idaho for reclamation bonding. If a company has a reclamation bond with the State of Idaho or the FS that can be used to perform reclamation on Federal leases, the amount of the bonding with these other agencies is taken into consideration when figuring the amount of additional bonding that may be required. A company may request a bond reduction if they are over bonded. However, companies who are over bonded may choose to remain over bonded to avoid negotiating a new amount with their surety company.

WO Comments: It appears that the bonds on file with BLM for P4 Production, LLC and FMC are in need of adjustment to cover at least 1/4 of the annual production/royalty. **Idaho reports in their comments on the draft report that these bonds are now in compliance. One bond was increased from $25,000 to $152,183 and the other lease in question was assigned to a company that has adequate statewide bonding on file. This lease is now covered by this larger bond.**

LR2000: Random check of serial register pages. Current data standards are being used in the cases checked.

Montana

Leases & Bonds

| Number of Leases | Producing Leases | Non-Producing Leases | Statewide Bonds | Individual Bonds | Leases In Default |
|---|---|---|---|---|---|
| 1 | 0 | 1 | 0 | 1 | 0 |

Bond Percent of Need

| Number of Bonds | Bond ≤24% of Need | Bond 25-49% of Need | Bonds 50-74 % of Need | Bonds 75-99 % of Need | Bonds ≥100 % of Need | Bonds/BLM < 100 % of Need Production/Royalty |
|---|---|---|---|---|---|---|
| 1 | 0 | 0 | 0 | 0 | 1 | 0 |

Montana's Comments:

The bond review process includes annual onsite visit to monitor reclamation requirements. The present bond is covers the annual rental requirement, or the minimum lease bond of $5000; plus any estimated reclamation costs.

WO comments: None

LR2000: Random check of serial register pages. It appears current data standards are being used.

New Mexico

Leases & Bonds

| Number of Leases | Producing Leases | Non-Producing Leases | Statewide Bonds | Individual Bonds | Leases In Default |
|---|---|---|---|---|---|
| 112 | 22 | 90 | 3 | 3 | 0 |

Bond Percent of Need

| Number of Bonds | Bond ≤24% of Need | Bond 25-49% of Need | Bonds 50-74 % of Need | Bonds 75-99 % of Need | Bonds ≥100 % of Need | Bonds/BLM < 100 % of Need (Production/Royalty) |
|---|---|---|---|---|---|---|
| 6 | 3 | 0 | 0 | 0 | 3 | 0 |

New Mexico's Comments: Bonding in the Non-Energy Leasable Minerals Program

The June 18, 2001 Evaluation Directive Letter states in part, "We need to conduct an evaluation of the bonding practices .to determine how we might correct any problems we identify in this program." and. "Program evaluations can also provide the information needed to develop specific policy changes." The attached work plan states "If States identify problems with their bonding program. then they should also identify any changes to BLM policies or regulations that would lead to a solution to these problems." In order to address bonding practice problems all serious problems must first be enumerated. This should be in the initial part of any successful evaluation.

We agree with the focus of this study, particularly with regard to program problem solving. We believe that the Objective section of the workplan should be expanded to include potential liability as well as liability. The work plan addresses liability as a quantifiable amount. That situation is not similar with regard to liability risk. Some examples of such risk include:

1. Possible BLM administrative errors in accepting reclamation and bonding assurance when one operator sells the operation to another. These situations are not always obvious, particularly when one is dealing with a situation described in item 2.

2. When the corporation holding an operation transfers fiscal responsibility from one of it's subsidiaries to another, particularly when the corporate structure contains shells.

3. Potential aftermath of corporate raiding or asset stripping, for example the Lundburg case.

4. When a bonding company leaves the business, or refuses to cover an increased bond.

Bonding processes and procedures are involved in potential liability. These are likely to be ignored if only calculated monetary liability is addressed.

Bonding process and procedural problems occur in all minerals programs. The oil and gas program has similar bonding issues on a much smaller scale, but with many more examples to study. A survey of problems of this nature in the oil and gas program would yield a statistically significant assessment of potential liability due to the much larger sample size. Such a survey could lead to a meaningful risk assessment on the whole bonding topic, and that could be a cornerstone of designing a better, safer, more efficient bonding process.

Bonding costs as a percentage of total operational cost industry-wide need to be examined, if these costs have a significant impact on royalty. If such costs escalate rapidly or are a significant percentage of operational costs, then reduced production of lower grade ores and lower profitability have a negative impact on royalty. High surety costs are a severely limiting factor for hardrock miners. Such costs generally limit the operator to small cash bonds. Because those operators are usually limited by bond constraints they are precluded from "Economy of Scale" operations. This results in inefficient and partial mining of many hardrock deposits due to regulatory requirements.

Mineral bonding issues transcend BLM mineral category boundaries. This evidences that the whole bonding system and process requires a major reform. Piecemealing will not solve the problem. However, demonstration projects into new approaches on bonding could lead us out of the bonding morass.

WO Comments: It appears that the bonds on file with BLM for IMC, Western-AG, MPI and Eddy Potash are in need of adjustment to cover at least 1/4 of the annual production/royalty.

LR2000: Random check of serial register pages. It appears current data standards are being used.

The scope of this evaluation is limited to the existing bonding program in the 3500 program. It is not intended to evaluate bonding in all BLM programs. This evaluation is not intended to evaluate the benefits or risks of relying on surety companies for bonds, or the cost of bonds to operators. This evaluation is intended to investigate if the states are complying with the bonding policy in this program as described in the regulations and the BLM manual. This evaluation does identify a problem with bonds in New Mexico and Utah. This is not persuasive evidence that the nation-wide policy is in need of revision. It appears that problems exist in some locations. The Washington Office is interested in working with the New Mexico State Office to help move these problem bonds closer to compliance with BLM policy. The use of surety bonds from a surety company on the list of approved sureties published by the Treasury Department will provide protection in situations 1, 2 and 3 described above. Item 4 can be successfully handled by transferring the bond to a new approved surety company. It is true that bonds can impact the lessees financial position, however, the cost of bonds is a required cost of operations. Increasing the use of concurrent reclamation can also reduce future liabilities, reducing the risks identified in items 1 through 4 above.

**Since the draft report was issued the Department has commissioned a task force to look at bonding for a variety of mineral commodities. This task force is a response to the emerging crisis in the availability of surety bonds needed to meet BLM's bonding requirements. This task force is looking at a much broader range of issues than is this evaluation. New Mexico's comments have been shared with the bonding task force since the comments also address a broad range of issues.**

Nevada

Leases & Bonds

| Number of Leases | Producing Leases | Non-Producing Leases | Statewide Bonds | Individual Bonds | Leases In Default |
|---|---|---|---|---|---|
| 2 | 2 | 0 | 0 | 2 | 0 |

Bond Percent of Need

| Number of Bonds | Bond ≤24% of Need | Bond 25-49% of Need | Bond 50-74 % of Need | Bonds 75-99 % of Need | Bonds ≥100 % of Need | Bonds/BLM < 100 % of Need (Production/Royalty) |
|---|---|---|---|---|---|---|
| 2 | 0 | 0 | 0 | 0 | 2 | 0 |

Nevada reported four additional leases; three prospecting permits and one BIA lease. These were not included in the evaluation because they were outside the scope of the report.

<u>Nevada's Comments:</u>

We refer in our bond estimation to the BLM Manual 3504, I, C, for producing leases.

WO Comments: None.

LR2000: Random check of serial register pages. Current data standards are being used in the cases checked.

<u>Utah</u>

Leases & Bonds

| Number of Leases | Producing Leases | Non-Producing Leases | Statewide Bonds | Individual Bonds | Leases In Default |
|---|---|---|---|---|---|
| 58* | 14 | 44** | 6 | 19 | 0 |

* Reported 69 leases but 3 were terminated. Terminated leases were not included in the evaluation. Eight additional leases were relinquished between the draft evaluation report and the final evaluation report so these 8 leases have been dropped from the evaluation.

** 17 of the Nonproducing leases are State Exchange Leases which are administered according to Utah State Rules and Regulations and are not bonded until development begins.

Bond Percent of Need

| Number of Bonds | Bond ≤24% of Need | Bond 25-49% of Need | Bonds 50-74 % of Need | Bonds 75-99 % of Need | Bonds ≥100 % of Need | Bonds/BLM < 100 % of Need (Production/Royalty) |
|---|---|---|---|---|---|---|
| 25 | 10 ++ | 0 | 0 | 1 | 14 | 1*** |

++ See comments below.
*** Bonds held by BLM are not adequate to cover 1/4 estimate annual production/royalty.
- Bond reviews in 1990,1997, and 2000.

Utah's Comments:

The Don Fulmer Clay lease was an exchange lease from the Utah State Institutional Trust Lands. The lease was not producing but has just started to produce again. This bond requires increasing for rents and royalties. The Utah Division of Oil Gas and Mining (UDOGM) in conjunction with BLM has required a bond for reclamation. This is in-place and held by the UDOGM.

++ Reilly Industries has ten potassium leases that require an additional $840,000 in bonding, mainly to cover reclamation costs. This is the only operator that is inadequately bonded at the present time. The bond estimate has been calculated and a meeting is pending with Reilly Industries on the bond issue.

Salada Minerals, LLC has eight sodium leases requiring an additional $506,000 in bonding, mainly to cover reclamation costs. At the present time they are not in production and they have chosen not to go into production in the near future. They cannot go into production until the reclamation bond is posted. February 2002 these leases will go into advance royalty status.
A letter to each of these lessees, requiring additional bonding, could be mailed in a week's time. However, it is our conclusion that none of the amounts on the producing properties would be paid without an appeal to IBLA and/or a court case. Our last appeal/court case with a coal lessee (5M) took almost four years to resolve, and this concerned rental payments on non-producing leases.

Initial requests for increased bonding would take approximately 20 work hours and $500 of the budget.

WO Comments: It appears that the bonds on file with BLM for case files UTU 02625, UTU 149937 and UTU 149938 are in need of adjustment to cover at least 1/4 of the annual production/royalty. **Utah responds that a decision increasing the bond for lease U-026255 to $7,000 was issued at time of readjustment. The lessee, Melvin Leslie has appealed that readjustment decision to IBLA. Utah also notes that the bonding for U.S. Steel Corp. Phosphate leases U-0149937 and 149938 combined is $194 short of being 100% bonded. A decision to increase the bond for each lease by $1,000 was mailed March 5, 2002 as a response to the draft evaluation report. WO notes that Utah is making progress in bringing all leases into full compliance with the bonding policies established in the 3504 manual.**

LR2000: Random check of serial register pages. Current data standards are being used in the cases checked.

Wyoming

Leases & Bonds

| Number of Leases | Producing Leases | Non-Producing Leases | Statewide Bonds | Individual Bonds | Leases In Default |
|---|---|---|---|---|---|
| 68 | 14 | 54 | 4 | 19 | 0 |

Bond Percent of Need

| Number of Bonds | Bond ≤24% of Need | Bond 25-49% of Need | Bonds 50-74% of Need | Bonds 75-99% of Need | Bonds ≥100 % of Need | Bonds/BLM < 100 % of Need (Production/Royalty) |
|---|---|---|---|---|---|---|
| 23 | 0 | 0 | 0 | 0 | 23 | 0 |

Wyoming's Bond Review Process/Comments:

The field inspector reviews each non-energy lease during the first quarter of each calendar year after receiving unit value figures from the Minerals Management Service. The bond amount is calculated to provide coverage for one year's rental and three month's production royalty. The required bond amounts are provided to the Branch of Solid Minerals and increase/decrease notices are then sent to the lessees.

Data Standards

A data cleanup effort for Wyoming non-energy leases was completed during 1998, in accordance with IM No. WO-97-79. We enter only the following four codes into Case Recordation:

300 - Bond Required
399 - Bond No Longer Required
465 - Bond Reviewed
909 - Bond Accepted

The entry of the bond accepted code into CR includes the Automated Bond Surety System (ABSS) bond number, which effectively ties the two systems together. Specific information pertaining to each bond is entered into the ABSS; therefore, there is very minimal duplication of data entry into CR and ABSS.

The current BLM bonding procedures have worked well for the Wyoming non-energy leasable program. We have not had a situation in the non-energy leasable program where we were required to collect on a bond. We feel that the Federal resource is adequately protected.

LR2000: Random check of serial register pages.  Current data standards are being used in the cases checked.

Appendix 2.
Data Summary Table

| State | Number of Leases P/NP * | Bonds ** ≤24% of Need | Bonds** 25-49% of Need | Bonds ** 50-74 % of Need | Bonds ** 75-99 % of Need | Bonds ** ≥100 % of Need | Total # of Bonds | Bonding *** % of Need | Bonds < 100 % of Need for Rent & Royalty | Leases in Default |
|---|---|---|---|---|---|---|---|---|---|---|
| AZ | 1/0 | | | | | 1 | 1 | 100% | | |
| CA | 2/7 | | | | | 6 | 6 | 100% | | 1 |
| CO | 5/3 | | | | | 5 | 5 | 100% | | |
| ES | 26/33 | | | | | 22 | 22 | 100% | | |

| | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| ID | 5/85 | | | | | 12 | 12 | 100% | | |
| MT | 0/1 | | | | | 1 | 1 | 100% | | |
| NM | 22/90 | 3 | | | | 3 | 6 | 50% | 3 | |
| NV | 2/0 | | | | | 2 | 2 | 100% | | |
| UT | 14/44 | 10 | | | 1 | 15 | 25 | 60% | 1 | |
| WY | 14/54 | | | | | 23 | 23 | 100% | | |

| | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| Total | 121/325 | 13 | | | 1 | 89 | 103 | 87% | 4 | 1 |

* P/NP ⇒ Producing/Non-Producing

** Bonding % of Need ⇒ Bond Amount /Annual Rental + Royalty (estimate 3 months royalty due) + Reclamation

** * Bonding % of Need ⇒ # of Bonds ≥75% + ≥100 % / Total # Bonds.